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Note title of the Amendment to

87TH CONGRESS } HOUSE OF REPRESENTATIVES { REPORT
2d Session } { No. 1638

AMENDMENTS TO THE ARMED SERVICES PROCUREMENT ACT OF 1947, CHAPTER 137, TITLE 10, UNITED STATES CODE

APR. 30, 1962.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

MR. HÉBERT, from the Committee on Armed Services, submitted the following

REPORT

[To accompany H.R. 5532]

The Committee on Armed Services, to whom was referred the bill (H.R. 5532) to amend the Armed Services Procurement Act of 1947, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

LEGISLATIVE HISTORY

The act of February 19, 1948 (62 Stat. 21), titled the "Armed Services Procurement Act of 1947," consolidated all of the laws then existing relating to military procurement.

It was the purpose of the Congress in this act to write into law all authority and limitations for procurement.

The act has not been substantially amended since enactment except for the addition of subsection (b) of 2305 on July 31, 1955 (Public Law 268, 84th Cong.), relating to advertized procurement and, again, in pertinent part to this bill by what were "mutually agreeable" changes in subsections 3 and 9 of section 2304, granting authority to negotiate contracts.

The limit of negotiated purchasing authority of $1,000 in subsection 3 was raised to $2,500; and subsection 9 had added to it nonperishable subsistence items in addition to perishable subsistence items. These amendments were contained in Public Law 85-599, act of August 6, 1958 (72 Stat. 514). The same act also amended section 2307 with reference to advance payments.

House Report 109, 80th Congress, 1st session, reporting H.R. 1366, on page 3, among other things, stated that it was the purpose of the act to cause the reestablishment of "the advertised competitive

method" in the placement of "the great majority" of contracts for supplies and services, and the committee report further declared that—

> this method gives the best assurance that suppliers in a position to furnish the Government's requirement will have a fair and equal opportunity to compete for a share in the Government's business.

It will be noted that the emphasis is upon formal advertising as a proven method and upon competition as a means of procuring Government supplies, with a fair and equal opportunity for suppliers and at prices brought about by competition in the market.

Then came the Korean hostilities, and, on December 15, 1950, the President issued a national emergency proclamation, which has not since been revoked. Immediately upon its issuance, the Secretary of Defense directed that all procurement be undertaken under the authority of section 2304(a)(1) of the Armed Services Procurement Act of 1941. This section permits negotiation of contracts during the period of a national emergency proclamation of the President. Such use of the national emergency authority in subsection (a)(1) effectively suspended the duties, limitations, and requirements specified in the other 16 exceptions where negotiation is permitted by the act of 1947.

Specifically, subsections 11 through 16 require that the use of the authority in these sections to negotiate have a requirement that the determination on the facts and the exercise of the authority be made at secretarial level, before such procurement may be undertaken. Others require reports to the Congress. All of them (11–16) were intended to restrict (except for the purpose specified in the exception) the negotiation of contracts for defense needs.

In 1955 and 1956, this committee, on inquiry, developed the fact that 94.19 percent of the defense procurement dollar was contracted for under the authority of the Presidential Korean National Emergency Proclamation (sec. 2304(a)(1)).

This represented round figure purchases of $34 billion as against $2 billion purchased by advertised competitive procurement. (However, in construction programs in the same period, 83 percent of the dollars of the U.S. Army Corps of Engineers and 72.9 percent of Navy's Bureau of Yards and Docks dollars were spent in advertised competitive procurement.)

The situation has improved, but not materially, since that time. Now we have fewer contractors, larger contracts, and relatively the same dollar volume of negotiated procurement.

After our hearings in 1957, we reported H.R. 8710 (H. Rept. 1688, 84th Cong., 2d sess.). It passed the House by a vote of 374 to 2. The Senate did not act. The first provision of that bill terminated the national emergency declared in 1950, insofar as it sanctioned negotiated procurement.

All that remains without statutory authority are the three unilateral set-aside programs and the authority to delegate responsibility which depend for their continued use upon the Korean National Emergency Proclamation.

It is the purpose of this bill to restore the rule of law to the military procurement processes and to add additional provisions which will strengthen the procurement methods because of the heavy incidence

of negotiated procurement for new and highly technical weaponry and supplies.

A more extensive review of the subject of procurement as a whole was made by the Armed Services Committee pursuant to the provisions of section 4 of the act of July 13, 1959, which directed the House and Senate committees to make such a study of methods, policies, and practices, and to consider the effectiveness of contractual instruments in achieving reasonable costs, prices, and profits in defense procurement.

Because of the extensive data assembled in that study, we refer to it for basic source material and only briefly outline here the detail developed in that report which became House Report 1959. As a result of developments and discussion during that study and inquiry, the committee believed it imperative that amendments be made to the Armed Services Procurement Act of 1947; that we msut restore the "rule of law" to defense procurement; and not depend upon regulations or emergency proclamations for the direction and guidance of a $24 billion procurement program.

In furtherance of its consideration, the committee reported H.R. 12572 (H. Rept. 1797, 86th Cong., 2d sess.). It passed the House by a voice vote, but the Senate did not act on the bill. The Senate, however, did issue a report as a result of its hearings pursuant to section 4, Public Law 86–89, which made findings in substantial agreement with the House, the difference being that the Senate, whose report was filed after adjournment, recommended that the subject matter be accompanied by regulation.

(H.R. 5532 is identical with H.R. 12572 which passed the House without dissent in the 86th Cong.)

SECTION ANALYSIS

Section (a)

Section (a) reaffirms the congressional intent and policy that formal advertising, the proven method of public procurement, shall be the rule, where it is feasible and practicable.

Heretofore, Congress has merely declared that formal advertising "shall be made." That has not been enough, in the way of a delaration of policy, as the Comptroller General has pointed out, to reduce the emphasis on procurement by negotiation through the 17 exceptions in the act and to accent normal, usual, and proven methods of advertised competitive procurement.

This is a section of policy. By this declaration of policy, specific actions are to be evaluated.

Section (b)

Section (b) of the bill restores to the Congress the authority to declare a national emergency which will suspend the restrictions, limitations, and requirements of the Armed Services Procurement Act of 1947.

Instead of continuing the Presidential authority such as is now provided by the Korean National Emergency Proclamation of December 16, 1950, this section will terminate emergency authority for negotiated procurement under this act. But the President's authority to declare a national emergency hereafter is neither curtailed nor circumscribed. Insofar as the authority to negotiate public purchases

is concerned, the authority for negotiated procurement other than as directed in exceptions 2 to 17 will be limited to another national emergency proclamation hereafter issued which the President may make. And, so far as procurement is concerned, that emergency will automatically terminate in 6 months after issue. This provision is intended to restore the procurement processes to such emergencies as may be declared by the Congress except for 6-month periods.

The provision will not forbid negotiation but will permit negotiation only when the specific requirements of exceptions 2 through 17 (sec. 2304(a)) will have been complied with. That is why we speak of this bill as restoring the "rule of law" to military procurement.

Section (c)

Section (c) of the bill amends subsection (14) of section 2304. It strengthens the language and limits the opportunities for negotiated procurement in such cases where the decision is based upon the requirement for "substantial initial investment or duplication in time for preparation." This provision is recommended by the Comptroller General for reasons presented to us during the hearing. It was assented to by the Department of Defense as a workable provision.

Section (d)

Section (d) amends exception 17 to give statutory authority and sanction for the negotiation of contracts on unilaterial set-asides by the Department of Defense in furtherance of small business, labor surplus, and disaster area programs.

This section depends upon the definition of small business as made by the Administrator of the Small Business Administration whose duties are prescribed by law; it limits procurements for the utilization of labor surplus to the places determined by the Secretary of Labor, who makes these determinations by law; and, finally, in areas where major disasters have occurred and been proclaimed by the President, then procurement by negotiation may be made to aid these areas. Depending upon the nature of the disaster, unilateral set-asides may be prescribed by the Department of Defense. There can be no additional cost to the military departments. The section is permissive only.

It must be carefully noted that this section takes note of the statutory responsibility of the three officers in charge of these various programs: An Administrator, a Secretary, and the President. The Defense Department is not required to purchase within the areas prescribed. But it does harmonize the actions of the Department of Defense with that of the public policy so that military procurement may be undertaken unilaterally within the broad spectrum of the administrative determinations concerning small business, labor surplus, and disaster areas. This authority is now being exercised only by virtue of the existence of the Korean National Emergency Proclamation. We put it in law.

Section (e)

Section (e) contains both direction and mandate with respect to negotiated procurement and the method by which it shall be conducted.

The Armed Services Procurement Act of 1947 did not define what should constitute negotiation. In the codification of 1958, the act was reworded to state that there were two categories of procurement,

by method: (1) Formal advertised sealed competitive bidding, and (2) negotiated procurement.

The problem has usually been one of interpreting what was meant by "negotiation."

This word is not defined in the statute. But the word does have a meaning in common parlance. It is that when negotiations are invited and proposals for negotiations are offered, there should be written or oral discussions.

The Military Establishment have not always been ready to grant that discussions should take place. This section provides (and it is not objected to by the Department of Defense and it was proposed by the Comptroller General) to emphasize not only the value but the necessity for written or oral discussions before final pricing and award of contracts when the proposers are within a competitive range, price and other factors considered.

This section likewise recognizes that where unilateral set-asides have been made, discussions are not necessary to the final determination. Competition as to price has already occurred, and the qualification of the concern is under one of the three set-aside programs already defined. Award, therefore, does not require discussions either as to price or performance. Discussions would be futile.

The section, however, gives authority, now being exercised with fewer restrictions in 3–805 of the Armed Services Procurement Regulations. Awards are now made without discussion, when the offerors have been notified in advance that final and firm proposals are to be made. Under this provision, such invitations may be issued only when there is a clear evidence of adequate competition or where there is accurate, prior cost experience with the product. This must be determined before award. The Comptroller General supported in principle and the Department of Defense supports this section.

It is a salutary and workable law which meets almost all requirements for negotiation; if not in language, at least by definition.

Section (f)

Section (f) is a correction in lettering of a subsection to accommodate a new section being added.

Section (g)

This, we believe, is one of the most important and useful provisions in the bill.

One of the contracts authorized to be employed under section 2306 of the Armed Services Procurement Act, when it shall have been determined to be "likely to be less costly," is the fixed-price-incentive-type contract. This type contract was used for 50 percent of Air Force dollars in 1959. It was used for 12 percent of Navy dollars in the same period.

It is most frequently employed in contractual relations with the airframe industry, now substantially the missile industry.

The contract is based upon the principle of sharing of profits where contractor's performance has allegedly resulted in cost reductions over the first expected price of the product.

The incentive contract originates in this way: After a prototype has been completed, it goes into the production quantity and a contract between the parties is formed. The Government "estimates"

the production costs and adds a normal profit (which usually turns out to be 8 percent). But the 8 percent is determined not in percentage (which would be a violation of section 2306 prohibiting cost-plus contracts), but it is a sum in dollars added to estimated costs in dollars by estimate culminating in fixing of what is known as a target price.

The target price is thus determined by "estimates" in "negotiations" before performance.

The contract provides that, when actual costs prove to be less than target price, the contractor will receive not only the sum in dollars which was "estimated" as "normal profit" but an "incentive profit" which is determined by the formula of paying the contractor 20 percent of each dollar of actual cost less than the first estimated target price.

If contractor's actual costs exceed the target price by 20 percent, the contractor loses no money but it does lose some profit. This is supposed to be an incentive to better the target price.

If contractor's actual costs exceed 120 percent of the target price, the contractor bears the cost.

This is pricing upon "estimate" and a determination of "profit on formula" rather than fact.

Since extra profits are presumptively an incentive for the risks assumed and the cost reduction achieved, these two things must be observed from experience. Air Force reporting on 171 contracts totaling $6,300 million had one instance where the ceiling price was exceeded and then only by $87,000.

In the Navy, of 47 contracts for $2,500 million, only one contractor paid $54,000 on a $4 million contract.

Thus, it would seem that the element of risk so far as the right to larger profits is concerned was not demonstrated.

In the case of the Air Force, the recovery was 3.2 percent and in the case of Department of Navy it was 2.7 percent.

But the real question is whether or not the difference between actual cost and target price is the product of sound and accurate negotiation or whether it may have been produced by misleading, misunderstood, or misapplied cost data. It was to this point that so many of the reports of the Comptroller General were directed.

Therefore, to restore this type of contracting to more accuracy in estimating target price, we would require full, complete, and accurate data and disclosure by both parties in pricing discussions.

The bill requires the contractor to certify to the cost figures in hand at the time of negotiations for target price. To the extent the negotiated "estimate" was inflated by inaccurate figures, an adjustment will be made before application of the price formula and final payment to eliminate from the target price inaccurate costs which may have got into the initial negotiation. Then a price formula will be more correctly applied, because the skill and initiative of the contractor will be more apparent in any claimed cost reduction.

This section, then, does two things: It requires by law a full disclosure in negotiations and it requires a readjustment of target prices, before final settlement and cost sharing, so that the incentive profit over the normal profit will be the product of the contractor's action in performance rather than artificial pricing in negotiations for target price.

This provision has the support of the Comptroller General, and it has at least the acquiescence of the Department of Defense.

But it does contain something the law does not now require: complete disclosure in negotiations and an agreement to readjust the target price for errors in overpricing.

Section (h)

Section (h) amends section 2310 of the act by requiring that the decisions and determinations required under exceptions 11 through 16 in section 2304, which require secretarial decisions, and section 2306(c), which requires the determination on the type of contract "likely to be less costly," and section 2307 requiring advance payments to be supported by written findings, to be written and to be clear and illustrative of the reasons for the action taken.

This will provide an opportunity for review and consideration of the administrative action taken.

The second part of the section provides that contracts negotiated under exception 2 (where the public exigency will not permit delay); exception 7 (for medicines and medical supplies); exception 8 (property for authorized resale); exception 12 (where the purchase should not be public); and the purchase of property for experiment, test, or research in exception 11, be supported by written findings which shall be preserved and may be reviewed.

These are administrative requirements and have for their purpose focusing attention of the executive department to the need for full consideration of the decisions to use these 16 exceptions by having a record in writing of the findings and determinations which can be reviewed.

This section, it is believed, will have a salutary effect.

Section (i)

Section (i) deals with the delegation to officers and officials of an agency of powers reserved to the Secretary except for determinations and decisions required under exceptions 11 through 16 of section 2304(a). This is an administrative provision to reduce administrative burdens.

The second portion of this section permits the delegation to an officer or official of an agency of the authority for procurement in research and development matters from the present limitation of $25,000 to $100,000.

This bill does not involve any appropriations or administrative costs.

COMMENTS OF THE DEPARTMENT OF DEFENSE AND THE COMPTROLLER GENERAL

GENERAL COUNSEL OF THE DEPARTMENT OF DEFENSE,
Washington, D.C., April 21, 1961.

Hon. CARL VINSON,
Chairman, Committee on Armed Services,
House of Representatives.

DEAR MR. CHAIRMAN: Reference is made to your request for the views of the Department of Defense on H.R. 5532, a bill to amend the Armed Services Procurement Act of 1947.

The Department of Defense recommends against the enactment of H.R. 5532 for the reasons set forth below. While certain provisions of the bill reflect current policies and practices of the Department as contained in its regulations, it is considered that enactment of such provisions into law is unnecessary and, with respect to certain other provisions, undesirable in that it would remove desirable flexibility in adapting these regulations to meet changing circumstances. As you know, following the study by the special Subcommittee on Procurement Practices of your committee last year and the reporting out of the committee and enactment by the House of H.R. 12572, this Department issued certain amendments to the Armed Services Procurement Regulation which generally conform with the objectives contained in H.R. 12572. Our objectives, we believe, are the same; formal advertising whenever practicable and feasible with increased effort being applied to placing more procurements by this method; a requirement for clear justification before the negotiated method of contracting is utilized; maximum practicable competition in negotiated procurements; and the establishment of appropriate safeguards to the Government in the negotiation of any contract where the price is based primarily on cost estimates rather than adequate price competition. There follows a detailed comment on the bill.

Title

The short title of the bill is "To amend the Armed Services Procurement Act of 1947." The Armed Services Procurement Act of 1947 is no longer appropriate for citation since the statute was repealed as a part of the codification of title 10, United States Code. The following is suggested in the interest of technical accuracy: "To amend chapter 137, title 10, United States Code."

Subsection (a)

Subsection (a) of the bill would amend section 2304(a) of chapter 137, title 10, United States Code, to state expressly the intent of Congress that all purchases of and contracts for property or services covered by the chapter should be made by formal advertising whenever such method is feasible and practicable under the existing conditions and circumstances. If such method is not feasible and practicable, the head of an agency, subject to certain determinations and findings being made, may negotiate such purchases or contracts under the 17 exceptions set forth in section 2304(a). Subject to subsequent comments on subsection (h) of the bill with respect to determinations and findings, the Department does not object to the purpose of this proposed amendment. However, in view of the fact that the objective of the proposed amendment has been accommodated by a revision to the Armed Services Procurement Regulation, it is considered that this amendment is unnecessary.

Subsection (b)

Subsection (b) would amend clause (1) of section 2304(a) in two respects. First, it would, in effect, preclude the use of the national emergency exception during the present emergency declared by the President. Secondly, in the case of a national emergency hereafter declared by the President, the period for use of the exception would be limited to 6 months following his declaration of such an emergency.

It is the view of the Department that the restriction on the use of

this authority in the case of a national emergency declared by the President is undesirable. As you know, use of this authority within the Department of Defense for the past several years has been confined to certain very limited areas. Recently, however, the authority proved invaluable in its application to the U.S. balance-of-payments problem. As you were informed by letter dated December 16, 1960, the Department after consultation with the General Accounting Office, determined to utilize the authority in connection with those proposed procurements brought back from abroad for award to domestic suppliers only. Since the procurements could not be made by formal advertising because of the exclusion of foreign bidders, clause (1) of section 2304(a) of title 10, United States Code, was the only authority available where the provisions of clauses (2) through (17) of that section were not applicable.

Subsection (b) of the bill, if enacted, would preclude the use of clause (1) for this purpose and also in future circumstances of a pressing nature which might arise during the period of the current national emergency or any future national emergency declared by the President beyond 6 months from the date of the declaration. It is the view of the Department that the authority of clause (1) should be preserved.

Subsection (c)

Subsection (c) would amend clause (14) of section 2304(a) so as to clarify the conditions under which negotiation is authorized by this section. The Department of Defense does not disagree with the objectives of these proposed changes. However, as you know, they have been substantially incorporated in the Armed Services Procurement Regulation and, accordingly, it is considered that changes to the law are unnecessary.

Subsection (d)

Subsection (d) of the bill would amend clause (17) of section 2304(a) of title 10 to authorize negotiation of contracts in furtherance of small business, labor surplus area, or major disaster area programs, which are now negotiated under clause (1). The Department does not object to the purpose of this amendment.

Subsection (e)

Subsection (e) would amend section 2304 by adding a new subsection (g) which would prescribe the following requirements as to all negotiated procurements in excess of $2,500 in which rates or prices are not fixed by law or regulation and in which time of delivery will permit:

(1) It would require that proposals be solicitated from the maximum number of qualified sources consistent with the nature and requirements of the supplies or services to be procured; and

(2) It would require that written or oral discussions be conducted with all responsible offerors who submit proposals within a competitive range, price, and other factors considered, with the exception of procurements in implementation of authorized set-aside programs, or of procurements where it can be clearly demonstrated from the existence of adequate competition or accurate prior cost experience that acceptance of an initial proposal without discussions would result in fair and reasonable prices.

With respect to the first requirement, it has always been the policy of the Department of Defense, and our regulations so provide, that in

negotiated procurement, proposals will be solicited from the maximum number of qualified sources of supplies or services consistent with the nature of an requirements for the supplies or services to be procured.

With respect to the second requirement, the Department believes that details with respect to the methods and techniques utilized in consummating negotiated contracts are best covered in departmental regulations which were revised recently to incorporate all the concepts contained in this subsection. Our experience indicates that changes are often necessary in this general area to cope with changing conditions or potential abuses. It would be difficult to keep the statute responsive to these changes.

Accordingly, while we do not object to the objectives of this subsection, we consider it preferable that the entire subject matter of this subsection continue to be handled by regulation rather than by statute and recommend, therefore, that this subsection be deleted from the bill.

Subsection (f)

Subsection (f) of the bill is a technical amendment conforming the language of section 2306(a) with the proposed amendment to be added by subsection (g) of the bill.

Subsection (g)

Subsection (g) of the bill adds a new subsection (f) to section 2306 which would provide that no contract negotiated under title 10 shall contain a profit formula that would allow the contractor increased fees or profit for cost reduction or target cost underruns, unless the contractor shall have certified that his cost data was current, accurate, and complete. There is an additional requirement for a contract provision by which the target cost or price would be adjusted to exclude any sums by which it may be found after audit that the target cost or price may have been increased as a result of any inaccurate, incomplete, or noncurrent data.

The Department of Defense has given careful and thorough consideration to this proposed addition to the statute and to the objective which it seeks to obtain. The Department is opposed to enacting this provision into law. While this subsection is directed at incentive contracts, the Department is of the opinion that its underlying purposes should be recognized without regard to the particular type of negotiated contract involved. Accordingly, the Armed Services Procurement Regulation currently requires the submission by a proposed contractor of a certificate in connection with the negotiation of any contract where the amount involves over $100,000 and the price negotiation is based more on the contractor's actual or estimated cost than on effective competition, established catalog or market prices, or prices set by law or regulation. In this certificate the contractor, subject to criminal penalties under section 1001 of title 18, United States Code, certifies to the best of his knowledge and belief that in the preparation of his proposal all actual or estimated costs or pricing data as of a prescribed date have been considered in preparing the price estimate, and made known to the contracting officer for use in evaluating the estimate. This certificate may also be required when procurements less than $100,000 are involved in particular cases where the contracting officer considers that the circumstances warrant such action.

In addition, as you were advised on January 19, 1961, there was adopted for publication as section 7-104.29 of the ASPR the following prescribed clause for insertion in any negotiated fixed-price-type contract which is expected to exceed $100,000 unless the contract price is based mainly on adequate price competition, established catalog, or market prices, or prices set by law or regulation:

"Price reduction for defective pricing data":

"(a) If the contracting officer determines that any price negotiated in connection with this contract was overstated because the contractor, or any first-tier subcontractor in connection with a subcontract covered by (c) below, either (i) failed to disclose any significant and reasonably available cost or pricing data, or (ii) furnished any significant cost or pricing data which he knew or reasonably should have known was false or misleading, then such price shall be equitably reduced and the contract shall be modified in writing accordingly.

"(b) Failure to agree on an equitable reduction shall be a dispute concerning a question of fact within the meaning of the 'Disputes' clause of this contract.

"(c) The contractor agrees to insert the substance of paragraph (a) of this clause in any of his subcontracts hereunder in excess of $100,000, unless the price is based on adequate price competition, established catalog, or market prices, or prices set by law or regulation."

The above contract provision may also be inserted in other contracts or modified to apply to additional subcontracts (including lower tier subcontracts) where the contracting officer considers that the circumstances of the particular case warrant such action.

It should be noted that the above ASPR provisions are broader than the provisions of the proposed new subsection (f) of section 2306 in that they would apply to other contracts besides the so-called incentive-type contract. It is planned, once experience has been developed under these clauses, to make any necessary changes for improvement which such experience may indicate. It is preferable, therefore, that such provisions be left to administrative regulation in lieu of embodying them in the statute.

Subsection (h)

Subsection (h) of the bill, among other things, would amend section 2310(b) to require that (1) with respect to findings made under clauses (11)-(16) of section 2304(a) that such findings be clearly illustrative of the conditions described in those clauses; (2) with respect to findings under section 2306(c) that they clearly indicate why the type of contract selected thereunder is likely to be less costly than any other type; and (3) with respect to findings under section 2307(c) that they clearly indicate why advance payments under that section would be in the public interest. The subsection also provides for finality as to each determination, decision, and finding required by the subsection. The Department does not object to these requirements. These requirements are already in our regulations. Amendment of the law would not appear to be required.

Subsection (h) would further amend section 2310(b) to require that contracts negotiated under clauses (2), (7), (8), (10), (12), and contracts for certain property under (11) of section 2304(a) shall be supported by written findings setting out facts and circumstances sufficient to clearly and convincingly establish that use of formal advertising would not have been feasible and practicable.

The Department is not opposed to written findings as required by this subsection with respect to clauses (2), (10), (12), and contracts for certain property under clause (11) of section 2304(a), and the Armed Services Procurement Regulation requires them. The Department, however, is opposed to the requirement for written findings as required by the subsection with respect to clauses (7) (medicine or medical supplies) and (8) (purchases for authorized resale). These exceptions generate a considerable volume of individual procurement actions. The Department feels that the requirement in the Armed Services Procurement Regulation requiring the use of formal advertising, where feasible and practicable, has introduced a new and important restriction on the use of these clauses. It is the Department's view that the imposition of written findings in these areas would not produce meaningful results and would introduce a heavy administrative burden on contracting officers.

The language of the subsection which reads "and for property or supplies under (11) of section 2304(a)" should be clarified. This provision is believed to be directed at the acquisition of supplies incident to the conduct of a research and development program. In its present form, the language could be construed as applying, for example, to a research contract under which a prototype model would be furnished. The Department does not feel that this result is desirable or intended. Accordingly, it is recommended that the subsection, if enacted, be revised by deleting from lines 8 and 9 of page 5 of the bill the words "property or supplies under (11) of section 2304(a)" and substituting in lieu thereof the words "standard commercial supplies under clause (11) of section 2304(a) that are to be used in connection with experiment, test, development, or research."

Subsection (i)

Subsection (i) of the bill would amend section 2311 to provide for the delegation of the power to make a determination or decision under section 2304(a)(11) to any officer or official who is responsible for procurement with respect to contracts requiring the expenditure of not more than $100,000. The Department favors the objective of this provision.

The Bureau of the Budget advises that, from the standpoint of the administration's program, there is no objection to the presentation of this report for the consideration of the committee.

Sincerely yours,

CYRUS R. VANCE.

COMPTROLLER GENERAL OF THE UNITED STATES,
Washington, April 17, 1961.

Hon. CARL VINSON,
Chairman, Committee on Armed Services,
House of Representatives.

DEAR MR. CHAIRMAN: Your letter dated March 14, 1961, requests our comments on H.R. 5532, 87th Congress, "A bill to amend the Armed Services Procurement Act of 1947."

The provisions of this bill are identical with those of H.R. 12572, which was passed by the House in the 86th Congress, and several of these provisions have been substantially incorporated into the

Armed Services Procurement Regulation since that time. While we view this action by the Department of Defense as a necessary step toward improvement of negotiation procurement practices, it is our opinion that the matters covered by this bill are basic to economical procurement. As such we believe the requirements imposed thereby should be made mandatory by legislation. In that regard we do not consider their inclusion in procurement regulations, which are subject to administrative revision without notice or review, as an adequate substitute for law. We therefore favor continued efforts by your committee to enact corrective legislation in these areas. With this in mind, we offer the following comments on the various provisions of the bill.

Section (a) would amend subsection 2304(a) of title 10, United States Code, to affirmatively state a requirement for use of formal advertising in all procurements in which the use of such method is feasible and practicable. In effect, this amendment would require the use of formal advertising, notwithstanding the existence of conditions described in one or more of the exceptions set out in subsections 2304(a)(1) through (17), unless the circumstances in any specific procurement are such as to make the use of formal advertising infeasible or impractical. We believe this subsection represents a necessary and desirable clarification of the intent and purpose of the present law. We therefore recommend its favorable consideration. We believe further, however, that its effectiveness in limiting use of the negotiation authority will be dependent upon the extent to which findings are required under section 2310, and the extent to which such findings will be subject to review. Further comments on this aspect of the problem are included in our remarks on subsection (h) of the bill.

Section (b) of the bill would amend the authority to negotiate contracts under subsection 2304(a)(1), so as to permit use of this authority only during emergencies declared by the Congress and during the first 6 months of emergencies declared by the President.

The present national emergency was declared by the President on December 16, 1950. Until recently, use of the subsection 2304(a)(1) negotiation authority has been limited to three classes of contracts: First, unilateral set-asides for small business firms; second, set-asides for disaster and surplus labor area programs; and, third, experimental, development, test, or research work with other than educational institutions where the contract is over $2,500 but not more than $100,000.

Since the present national emergency was declared by the President more than 10 years ago, enactment of section (b) of the bill would preclude use of the national emergency negotiation authority for any procurement until a new emergency is declared by Congress or by the President. Section (d) of the bill would therefore authorize the negotiation of small business, labor surplus area, or major disaster area procurements under section 2304(a)(17), while section (j) of the bill would amend section 2311 so as to authorize the delegation of authority to negotiate contracts up to $100,000 for experimental, development, test, or research work.

We have no reason to disagree with the justification or necessity for negotiating these procurements. However, the fact that the present emergency has been prolonged for more than 10 years, during which time the need to negotiate these classes of procurements has

continued to exist, would appear to raise some doubt as to whether the authority to continue their negotiation should depend upon the existence of a national emergency. We are therefore inclined to favor the enactment of specific permanent legislation such as is here proposed, to authorize negotiation of these classes of procurements. With such amendments it would appear that no present need for the use of the national emergency negotiation authority would exist. Consequently, to the best of our knowledge, the amendments proposed by sections (b), (d), and (j) would impose no present hardship on the military departments. The amendments would, however, retain the authority of the President to again invoke the national emergency negotiation authority in the event such need should arise during a period when Congress was not in session.

We therefore favor enactment of these portions of the bill.

Section (c) of the bill would amend section 2304(a)(14) so as to require an additional determination that formal advertising would result in excessive cost to the Government by reason of duplication of a substantial initial investment, before negotiation of a contract could be justified on that basis.

Section 2304(a)(14) now authorizes negotiation where it is determined that manufacture of the supplies will require a substantial initial investment and that use of formal advertising might require duplication of such investment. During fiscal year 1960 over $6 billion, amounting to more than 30 percent of the total defense procurement dollars, were obligated by contracts negotiated under exception (14). The legislative history indicates that the authority in exception (14) was considered necessary because adherence to formal advertising procedures in the procurement of aircraft, missiles, radar, tanks, etc., would consistently result in the United States being 1 to 2 years behind latest developments. We agree that negotiation may be necessary and desirable in many instances involving procurement of these types of equipment, and that a substantial increase in leadtime which may be required by a contractor who must duplicate preparation already made by another contractor would, in some cases, justify negotiation on a sole-source basis.

However, merely because a substantial initial investment has already been made by one contractor, and such investment would have to be duplicated if a contract were awarded to a different contractor, does not, in our opinion, furnish sufficient justification for either failure to advertise or for negotiating on a sole-source basis. Where leadtime is a material factor we agree that authority to negotiate may be necessary to protect the national security interest. But we see no real justification or necessity for failing to advertise, where leadtime is not a material factor, simply because such method might require duplication of investment, unless such duplication would result in excessive cost to the Government. We therefore agree with the amendment proposed in section (c) of the bill.

Section (d) of the bill is designed to provide permanent negotiation authority for those procurements presently being negotiated under the national emergency authority of subsection 2304(a)(1).

We understand that the subsection 2304(a)(1) authority has recently been invoked to eliminate foreign competition in the procurement of supplies for use abroad, and that such use is considered necessary because this objective cannot be accomplished under exceptions (2)

through (17). We have not had the opportunity to examine these procurements and we are not in a position to render an informed opinion in the absence of such examination. However, if such procurements do, in fact, represent a necessary and justifiable use of the negotiation authority, we do not believe its availability should be dependent on the existence of a national emergency, and we would be inclined to recommend that it be considered for inclusion in section (d) of the bill, rather than to view it as justification for indefinite continuation of the present exception (1) authority. Otherwise, we recommend favorable consideration of section (d) of the bill in its present form.

Section (e) of the bill is designed to require the conduct of written or oral discussions with a representative number of suppliers in all negotiated procurements where such negotiation might reasonably be expected to serve the interest of the Government.

Other than that portion of this section beginning on line 22, page 3, of the bill, which would provide that no written or oral discussions are required in certain negotiated procurements where the request for proposals notifies all offerors of the possibility that award may be made without discussion, we recommend favorable consideration of section (e).

With respect to the exemption from written or oral discussions set out in line 22, page 3, through line 3, page 4, of the bill, we understand this exemption is in accordance with the opinion of the Department of Defense that, if there is a reasonable basis for believing that negotiation discussions will be had with all offerors, bid proposals will frequently contain allowances for contingencies and would usually be considerably higher than the offeror would ultimately be willing to negotiate. The Department feels that if the right is reserved to make an award without discussions, the offerors will then submit their best price proposals at the outset.

While this position may well have merit under the law as presently constituted, we question its merit under the provisions of this bill. Thus, section (e) would require written or oral discussions only with such offerors as may initially submit offers within a competitive range. The fact that an offeror must be within the competitive range in order that his proposal be the subject of further negotiations would, we believe, elicit initial responsive bids relatively free of abnormal contingency factors and thereby overcome the Department's argument that the right to award without negotiation must be reserved to force responsive initial proposals. Moreover, effective negotiations should identify any remaining unwarranted allowances for contingencies.

We believe discussions with all offerors within a competitive range is the essence of sound negotiation procedures and is essential to achieving the most favorable prices for the Government. We therefore recommend amending the bill by inserting a period immediately following the word "programs" in line 22, page 3, and deleting the remaining portion of section (e). In any event, we believe the word "or" in line 24, page 3, of the bill should be changed to "and."

Section (f) of the bill is a technical change relating to the provisions of section (g).

Section (g) of the bill covers limitations on profit formulas in negotiated incentive-type contracts. We agree with the objectives

of this section and particularly favor its provision which would require all incentive contracts to provide for an adjustment to exclude any sums by which it may be found after audit that target cost or price may have been increased as a result of inaccurate, incomplete, or noncurrent data. However, we believe the section should go further and provide that additional fees or profits for reductions of costs below negotiated targets should be limited to those reductions which are attributable to some effort on the part of the contractor to earn such additional fees or profits. Under section (g) as presently written it would appear that the contractor could participate in all reductions, regardless of how generated, except those which are a result of initial targets having been based on inaccurate, incomplete, or noncurrent cost data. Also, we are of the opinion that it should be incumbent upon the contractor to demonstrate his entitlement to additional incentive fees or profits, whereas section (g) would require the Government to demonstrate that a contractor is not entitled to additional incentive fees or profits.

In addition, it is not entirely clear from the language of section (g) whether initial target costs or profits which include estimates based upon price estimates or preliminary quotations from subcontractors would be interpreted as being subject to adjustment if, at a later date, it is found that the initial subcontract prices or quotations were inaccurate, incomplete, or noncurrent at the time of negotiation or that the subcontractor, at some later date, had voluntarily reduced its prices through no effort on the part of the prime contractor to obtain such reduced prices.

We have given further consideration to this problem since our report to your committee on H.R. 86-12299 and now recommend that a provision substantially as follows be substituted for the language presently proposed by section (g) of the bill.

"(f) No incentive-type contract shall be negotiated under this title unless the incentive profit formula contained therein would reward the contractor only for cost reductions accomplished by improved methods, practices, and techniques in the manufacture, production, fabrication, or assembly of the items, including any economies achieved in labor, material, or overhead costs not otherwise predictable as a result of prior production experience: *Provided*, That in no event shall additional fees or profits be allowed for cost reductions or target cost underruns resulting from voluntary reductions in subcontract prices or from use at the time of negotiations of cost data or other information that was incomplete, inaccurate, or noncurrent, including the use of subcontract prices based on incomplete, inaccurate, or noncurrent data. Such negotiated contracts shall contain a provision that the target cost or price shall be adjusted on the basis of an audit to exclude any net sums by which the target cost or price may have been overstated as a result of inaccurate, incomplete, or noncurrent data or information."

Section (h) would amend 2310(b) so as to impose additional requirements that the written findings made by agency heads in support of decisions and determinations to negotiate under exceptions (11) through (17), to use cost-type contracts, or to make advance payments, must set out sufficient facts and circumstances to clearly justify the decision or determination. It would also require that negotiation by subordinate officials under exceptions (2), (7), (8), (10),

and (12) be supported by written findings setting out facts and circumstances sufficient to clearly and convincingly establish that use of formal advertising was not feasible and practicable. Additionally, it would provide that such findings, both when made by contracting officers or other subordinate officials under exceptions (2), (7), (8), and (10), as well as by the agency head under exception (12), shall be final.

To the extent that the finality accorded by the present law to findings and determinations by the head of an agency would not only be continued under the provisions of section (h), but such finality would also be accorded to findings made by contracting officers under exceptions (2), (7), (8), and (10), we are unable to agree with these provisions. Our reasons for this disagreement are set out below and, based thereon, we feel strongly that favorable consideration should not be given section (h) in its present form.

The finality provisions of section 2310 at the present time are applicable only to findings, decisions, and determinations which are required to be made by the agency head. These are as follows:

1. A determination that negotiation under section 2304(a)(1) is necessary in the public interest during a period of national emergency.

2. Determinations, and findings in support thereof, to negotiate under section 2304(a) (11) through (16).

3. A determination under section 2306(c), and findings in support thereof, that use of a cost, cost-plus-a-fixed-fee, or incentive-type contract is likely to be less costly to the United States than any other kind of contract, or that it is impracticable to obtain property or services of the kind or quality required except under such a contract.

4. A determination, and findings in support thereof, to make advance payments under section 2307.

The legislative history of section 2310 clearly indicates that the finality given to determinations and decisions by the agency head was intended to prevent their being challenged by either the Comptroller General or the courts. But it was the opinion of the committees of both Houses that, while determinations and decisions by officials other than the agency head reasonably supported in fact and law should be final, power should be retained in the Comptroller General to examine and question contracts negotiated under such determinations. The Comptroller General was therefore advised in the report of both committees to take appropriate action on negotiated contracts which did not involve determinations by an agency head and where there was a question as to the legality of the action taken or evidence of abuse of the negotiating authority. In view thereof, it would appear to be clear that the Comptroller General has the authority under the present law to examine into the facts and circumstances relied upon by subordinate officials of an agency to support the negotiation of contracts under exceptions (2) through (10) and under exception (17) and, where use of the negotiation authority is not supported in fact or law, or where there is evidence of abuse of the negotiation authority, to pass upon the legality of the contract awarded.

To the extent that section (h) of H.R. 5532 would give finality to findings made by subordinate officials in support of determinations to negotiate under exceptions (2), (7), (8), and (10) it is our opinion that the Comptroller General, in the event of enactment of section (h) in its present form, would be effectively precluded from

taking any action, other than a formal report to the Congress, based upon abuse or illegal use of these exceptions. Once the findings were made final by operation of law, the facts and circumstances set out therein, though clearly erroneous, would not be subject to question. And if the findings on which a determination was based are final, it would be futile to attempt to question the determination itself.

We are of the opinion that the finality which now attaches to determinations of the agency heads on the use of exceptions (11) through (16), on determinations to negotiate a class of contracts, and on determinations to use cost-type contracts, has been a major contributing factor to the substitution of negotiation for formal advertising in defense procurements. To now add finality to findings made by subordinate officials in negotiating under exceptions (2), (7), (8), and (10) will only contribute further to this trend.

Under an advertised procurement, Government agencies are required to determine the lowest responsible bidder and award the contract on that basis. Since 1921 the General Accounting Office has reviewed the facts and figures relied upon by the contracting agencies in making these determinations. Where the facts were in error or the determinations were clearly not supported by the facts, we have advised the agencies that awards based upon such determinations would be contrary to law and therefore could not be recognized as valid obligations of the United States. This involves correcting administrative determinations which are clearly erroneous or unsupported by the facts. We see no material difference between such a review and a similar review of the facts and figures relied upon by the head of an agency to support his determination that a cost-type contract is likely to be less costly than any other type; the facts relied upon to justify the determination that it is necessary to negotiate all contracts contemplated by a class determination; or that the facts relied upon to negotiate under exceptions (11) through (16) do exist and that such facts are of the nature contemplated by the exception to be used. Finality of determinations by an agency head can be justified only where lack of finality would result in the General Accounting Office, the courts, or the Congress substituting its judgment for that of the agency head. But there is no justification for according finality to a determination by an agency if such determination is clearly erroneous. This is the case where the actual facts are other than as shown in the findings, or where the findings of fact are correct but such facts clearly do not meet the criteria set out in the law which the agency head is relying upon to support his action.

We feel that the blanket immunity from effective review and the resulting lack of accountability for the propriety of contract awards, which is conferred by the present finality provisions of 10 U.S.C. 2310, is unnecessary to efficient and effective procurement and operates as an open invitation to negotiate contract awards which are contrary to the intent of the law.

We recognize our authority and responsibility under the law to report abuses of the negotiation authority to the Congress. Unfortunately, reports of this nature must usually be made on an after-the-fact basis. We believe effective control of negotiated procurement practices must include authority for an independent review of the facts in each procurement before, as well as after, the procurement becomes an accomplished fact.

While we recognize that the extent and nature of the review which is to be given negotiated procurements involving a determination by the head of an agency is a question of policy to be decided by the Congress, we believe additional authority for congressional review of negotiated procurements. rather than less authority as proprosed by section (h) of the bill, is necessary and desirable. We therefore not only recommend against the extension of finality proposed by section (h) but also recommend that the provision of 10 U.S.C. 2310 be amended so as to deny finality to the findings and determinations of agency heads where such findings and determinations are clearly erroneous or are not supported by the facts. We therefore strongly urge that section (h) be amended by deleting the phrase "shall be final and" from line 14, page 5, of the bill.

Additionally, we recommend that section (h) of the bill be redesignated as section (i) and that a new section (h) reading as follows be inserted into the bill:

"(h) Subsection 2310(a) is amended to read as follows:

"(a) Determinations and decisions required to be made under this chapter by the head of an agency may be made for an individual purchase or contract or for a class of purchases or contracts. Unless such determinations and decisions are based upon erroneous findings of fact or are not supported by the facts, they shall be final."

We have no objection to the provisions of the present section (i) of the bill.

Sincerely yours,

JOSEPH CAMPBELL,
Comptroller General of the United States.

CHANGES IN EXISTING LAW

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, there is herewith printed in parallel columns the text of provisions of existing law which would be repealed or amended by the various provisions of the bill:

EXISTING LAW	THE BILL
Act of February 19, 1948 (62 Stat. 21)	
Section 2304	Section 2304
(a) Purchases of and contracts for property or services covered by this chapter shall be made by formal advertising. However, the head of an agency may negotiate such a purchase or contract, if—	(a) Purchases of and contracts for property or services covered by this chapter shall be made by formal advertising in all cases in which the use of such method is feasible and practicable under the existing conditions and circumstances. If use of such method is not feasible and practicable, the head of an agency, subject to the requirements for determinations and findings in section 2310, may negotiate such a purchase or contract, if—.

EXISTING LAW	THE BILL
Section 2304(a) (1) it is determined that such action is necessary in the public interest during a national emergency declared by Congress or the President;	Section 2304(a) (1) it is determined that such action is necessary in the public interest during a national emergency declared by the Congress or for a period of six months following a national emergency hereafter declared by the President.
Section 2304(a) (14) the purchase or contract is for technical or special property that he determines to require a substantial initial investment or an extended period of preparation for manufacture, and for which he determines that formal advertising and competitive bidding might require duplication of investment or preparation already made or would unduly delay the procurement of that property;	Section 2304(e) (14) the purchase or contract is for technical or special property that he determined to require a substantial initial investment or an extended period of preparation for manufacture, and for which he determines that formal advertising would be likely to result in additional cost to the Government by reason of duplication of investment or would result in duplicate of necessary preparation which would unduly delay the procurement of the property;
Section 2304(a) (17) negotiation of the purchase or contract is otherwise authorized by law.	Section 2304(a) (17) otherwise authorized by law, or when in furtherance of small business, labor surplus area, or major disaster area programs, the agency head determines that supplies or services are to be procured from small business concerns as defined by the Administrator of the Small Business Administration, from concerns which will perform the contracts substantially within labor surplus areas as determined by the Secretary of Labor, or from concerns which will perform the contracts substantially within areas of major disaster as determined by the President.
(None.)	(New.) Section 2304 (g) In all negotiated procurements in excess of $2,500 in which rates or prices are not fixed by law or regulation and in which time of delivery will permit, proposals shall be solicited from the maxi-

EXISTING LAW

THE BILL

mum number of qualified sources consistent with the nature and requirements of the supplies or services to be procured, and written or oral discussions shall be conducted with all responsible offerors who submit proposals within a competitive range, price, and other factors considered: *Provided, however*, That the requirements of this subsection with respect to written or oral discussions need not be applied to procurements in implementation of authorized set-aside programs or to procurements where it can be clearly demonstrated from the existence of adequate competition or accurate prior cost experience with the product, that acceptance of an initial proposal without discussion would result in fair and reasonable prices and where the request for proposals notifies all offerors of the possibility that award may be made without discussion.

(f) The second sentence of subsection 2306(a) is amended by substituting "(f)" for "(e)".

Section 2306. KINDS OF CONTRACTS.

(a) The cost-plus-a-percentage-of-cost system of contracting may not be used. Subject to this limitation and subject to subsections (b)–(e), the head of an agency may, in negotiating contracts under section 2304 of this title, make any kind of contract that he considers will promote the best interests of the United States.

Section 2306

(f) No contracts shall be negotiated under this title containing a profit formula that would allow the contractor increased fees or profits for cost reductions or target cost underruns, unless the contractor shall have certified that the cost data he submitted in negotiations for the fixing of the target cost or price was current, accurate, and complete; and such contracts shall contain a provision that the target cost or price shall be adjusted to exclude any sums by which it may be found after audit that the target cost or price may have been increased as a result of any inaccurate, incomplete, or noncurrent data.

EXISTING LAW	THE BILL
Section 2310. DETERMINATIONS AND DECISIONS.	Section 2310
(b) Each determination or decision under clauses (11)–(16) of section 2304(a), section 2306, or section 2307(c) of this title shall be based on a written finding by the person making the determination or decision. Such a finding is final and shall be kept available in the agency for at least six years after the date of the determination or decision. A copy of the finding shall be submitted to the General Accounting Office with each contract to which it applies.	(b) Each determination or decision under clauses (11)–(16) of section 2304(a), section 2306(c), or section 2307(c) of this title shall be based on a written finding by the person making the determination or decision, and such findings shall set out facts and circumstances which (1) are clearly illustrative of the conditions described in clauses (11)–(16) of subsection 2304(a), or (2) clearly indicate why the type of contract selected under subsection 2306(c) is likely to be less costly than any other type, or (3) clearly indicate why advance payments under subsection 2307(c) would be in the public interest. Contracts negotiated under clauses (2), (7), (8), (10), (12) and for property or supplies under (11) of section 2304(a) shall be supported by a written finding setting out facts and circumstances sufficient to clearly and convincingly establish that use of formal advertising would not have been feasible and practicable. Each determination, decision, and finding required by this subsection shall be final and shall be kept available in the agency for at least six years after the date of execution of the contract to which it applies, and a copy thereof shall be submitted to the General Accounting Office with each contract to which it applies.

EXISTING LAW

Section 2311. DELEGATION

The head of an agency may delegate, subject to his direction, to any other officer or official of that agency, any power under this chapter except the power to make determinations and decisions under clauses (11)–(16) of section 2304(a), of this title. However, the power to make a determination or decision under section 2304(a)(11) of this title may be delegated only to a chief officer or official of that agency who is responsible for procurement, and only for contracts requiring the expenditure of not more than $25,000.

THE BILL

Section 2311. DELEGATION

The head of an agency may delegate, subject to his direction, to any other officer or official of that agency, any power under this chapter except the power to make determinations and decisions under clauses (11)–(16) of section 2304(a), of this title. However, the power to make a determination or decision under section 2304(a)(11) of this title may be delegated to any other officer or official of that agency who is reponsible for procurement, and only for contracts requiring the expenditure of not more than $100,000.

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